



Leather

Sector Study



- Leather is one of the most widely traded commodities globally. The popularity of leather in various industries comes from its high tensile strength, good heat insulation, flexibility and durability.
- The primary raw material for leather industry is derived from slaughter houses and waste from the meat industry. This raw material is processed and converted into usable leather in tanneries. Hence, tanning industry is considered as one of the primary leather processing units in the entire leather industry.
- The demand in leather industry is driven by the fashion industry that includes footwear, garments, bags and belts. Apart from this, furniture and automotive industry also demand leather. The broad categories of leather industry include:
- **Tanned leather:** Leather produced from treating skins and hides of animals
- **Garments:** includes leather jackets, long Coats, waist coats, pants, and accessories such as gloves.
- **Footwear:** includes formal footwear, boots, sandals and clogs with leather uppers for both men and women.
- **Bags and Belts:** includes wallets, handbags, backpacks, cosmetic cases, laptop bags and leather belts.
- **Furniture:** majorly used for furniture covers.
- **Automotive:** majorly used for car interior, especially seat covers.

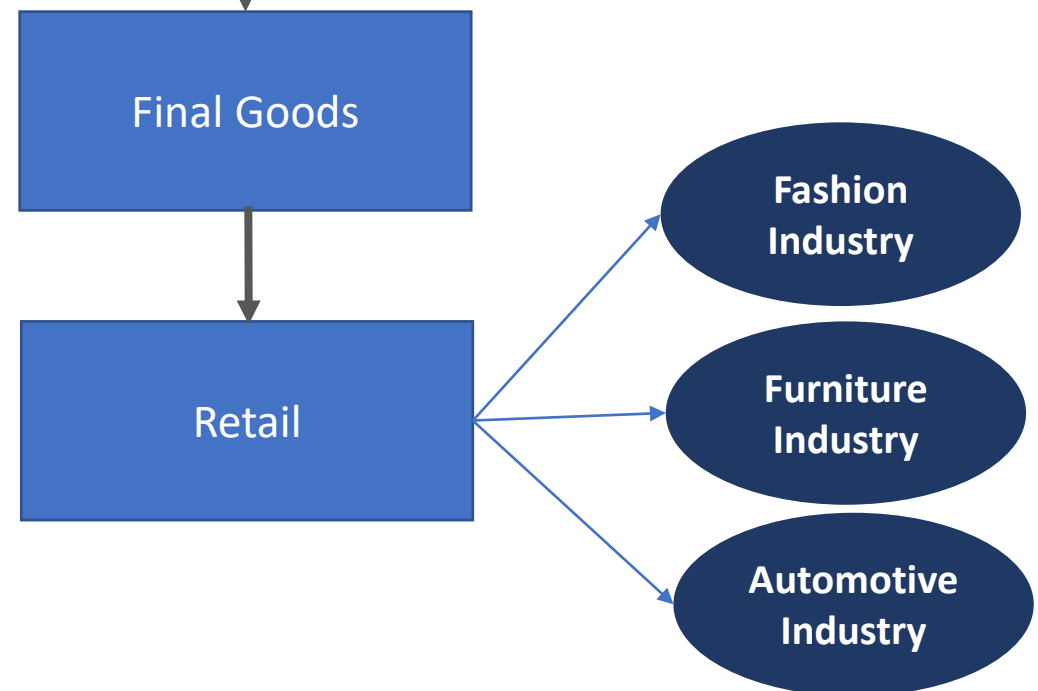
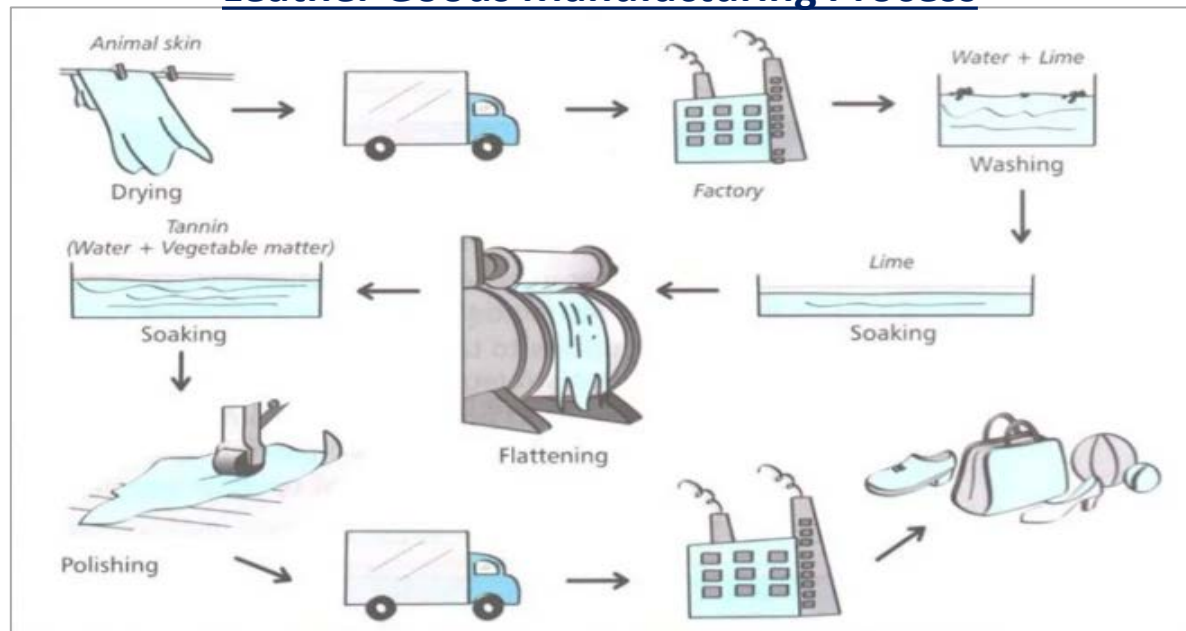


LEATHER | INTRODUCTION

Production Process



Leather Goods Manufacturing Process





Overview

- The global leather industry consisting of tanned leather, leather garments, gloves, bags & belts and footwear grew by ~6% YoY and reached a value of USD~370bln in CY21 (USD~351bln in CY20).
- Approximately USD~34bln of leather and leather products were traded globally in CY20. Tanned leather was the highest traded product, making up ~22% of the total trade, followed by leather garments (~19%), gloves (~4%) and footwear (~2%).
- Europe is the largest consumer of leather goods because of the strong presence of fashion-driven countries, such as France and Italy, product and technological innovations, rise in disposable income and online retailing.
- The Asian leather market is expected to witness fastest growth in the coming years due to presence of large number of leather product manufacturers in the region. Currently, China produces 67% of the world's shoes and exports 36% of its leather products.
- Factors such as high cost of leather products and absence of developed supply chain in many major exporting countries is expected to hamper the growth of global leather market. However, increasing investment by well-known luxury brands and approach towards rising trends development, such as bio-leather products, are factors that are expected to create a whole new world of opportunities in the global leather industry.

Global Overview	CY20	CY21
Market Size (USD bln)	350.7	370.0
Leather Trade - CY20 (USD bln)		
Tanned Leather	7.2	
Leather Garments	6.3	
Leather Gloves	1.3	
Leather Footwear	0.7	
Others	18.0	
Total	33.6	

Exports

- The top ten countries collectively account for ~75% of the total global exports, where China alone contributes ~21% to the total, followed by Italy (~14%). Other major exporters include India, Germany and Hong Kong.

Top Exporters - CY20 (USD '000)

Tanned Leather		Garments		Leather Gloves		Leather Footwear	
Italy	2,123,525	Italy	1,126,852	China	434,907	China	208,649
Brazil	556,862	China	823,972	Pakistan	225,195	Dominican Republic	120,469
China	497,230	India	602,636	India	179,692	Italy	63,012
Hong Kong	419,201	France	567,266	Germany	54,282	Singapore	39,682
Thailand	382,759	Pakistan	541,831	Sweden	35,959	Germany	29,842
Germany	313,203	Germany	363,045	Belgium	35,823	UAE	22,561
Austria	289,688	Netherlands	196,285	Bangladesh	30,453	Belgium	17,037
Vietnam	282,032	Hong Kong	192,904	Netherlands	28,582	Spain	14,637
India	255,945	Spain	179,061	France	22,147	Vietnam	14,577
Korea	210,951	UK	153,169	USA	22,067	Portugal	14,569
Other	1,894,180	Other	1,546,524	Other	244,160	Other	172,012
Total	7,225,576	Total	6,293,545	Total	1,313,267	Total	717,047

Imports

- USA is the biggest importer of leather and leather products, making up ~11% of the global imports, whereas Germany comes in second with ~6% share. Other major importers include France and Vietnam.

Top Importers - CY20 (USD '000)							
Tanned Leather		Garments		Leather Gloves		Leather Footwear	
Vietnam	869,929	USA	1,084,865	USA	311,963	Germany	62,990
China	781,743	Germany	556,266	Germany	109,461	USA	27,798
Hong Kong	435,314	France	473,423	Canada	90,519	Poland	25,444
USA	353,359	Italy	332,271	France	67,660	UK	23,666
Indonesia	276,336	China	329,124	Japan	63,694	France	19,432
Mexico	272,275	UK	287,599	Sweden	46,659	Vietnam	15,000
Germany	265,442	Japan	240,387	UK	41,790	Belgium	14,069
Italy	251,556	Netherlands	227,338	Netherlands	38,025	Singapore	12,527
Romania	229,394	Hong Kong	217,894	Belgium	36,570	UAE	10,328
Poland	221,427	Korea	184,334	Poland	33,057	Korea	9,885
Other	3,268,801	Other	2,360,044	Other	473,869	Other	495,908
Total	7,225,576	Total	6,293,545	Total	1,313,267	Total	717,047



LEATHER | LOCAL INDUSTRY

Overview

- Pakistan’s leather industry earned a revenue of PKR~133bln in FY21 (USD~833mln), showing a growth of ~10% year-on-year as the international trade resumed in FY21 after the COVID-19 hit.
- According to the Pakistan Tanners Association (PTA), Pakistan leather industry is ~95% export-oriented. Exports clocked in at PKR~133bln in FY21, up from PKR~120bln in FY20, depicting a growth of ~11%. Leather industry exports account for almost ~3% of total country’s exports.
- The leather exports of the country observed this growth as there was a ~18% increase in the average unit price per square meter of tanned leather to USD~12.9 in FY21 (USD~10.9 in FY20). Moreover, export volumes also increased during the year. Volume of leather garments registered an increase of ~29% while gloves and footwear surged by ~37% and ~22% respectively.
- However, the sector has seen a declining trend in the last few years. Leather exports stood at PKR~131bln in FY14 as compared to PKR~96bln in FY17. The main reasons behind the decline were delays in collection of fresh hides and skins particularly during Eid-ul-Adha, combined with absence of modern preservation techniques to avoid spoilage. This trend reversed in FY18 due to the export-friendly government policies.

Local Overview		
	FY20	FY21
Market Size (~USD mln)	765	833
Market Size (~PKR bln)	121.2	133.7
Exports (~PKR bln)	120.4	133.3
No of players	~800 tanneries and 4 listed companies	
Exports Volume		
Leather Garments ('000 Sq. M)	1,002	1,288
Leather Gloves ('000 Dozen)	5,061	6,911
Leather Tanned ('000 Sq. M)	16,915	12,558
Leather Footwear ('000 Pairs)	6,587	8,034
Industry Association		
<ul style="list-style-type: none"> • Pakistan Tanners Association (PTA) • Pakistan Leather Garments Manufacturers and Exporters (PLGMEA) • Pakistan Footwear Manufacturers Association (PFMA) 		

LEATHER | LOCAL INDUSTRY

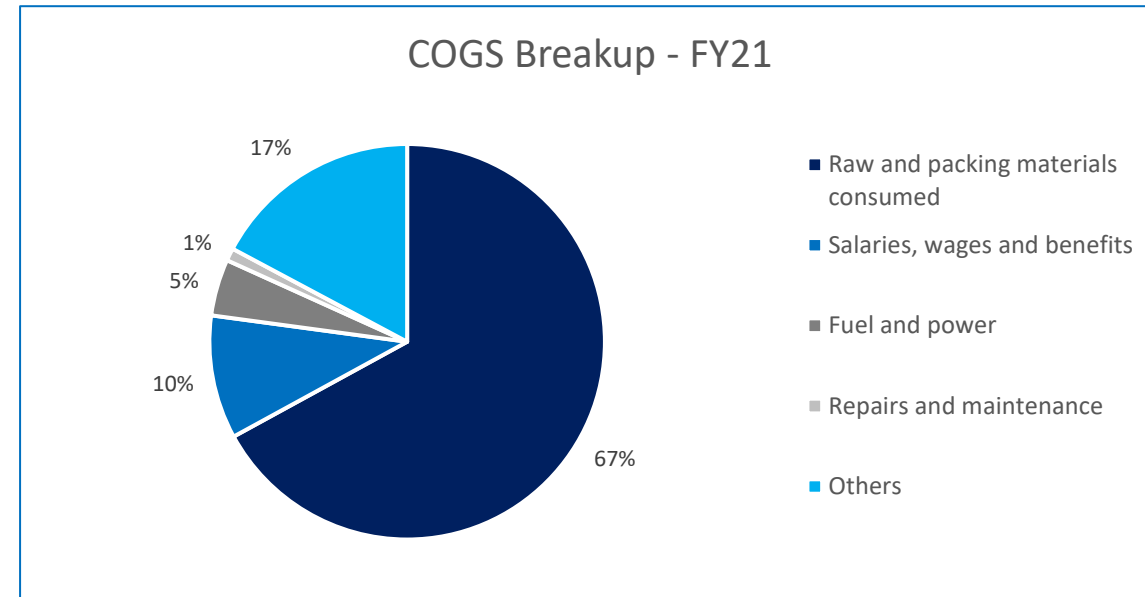
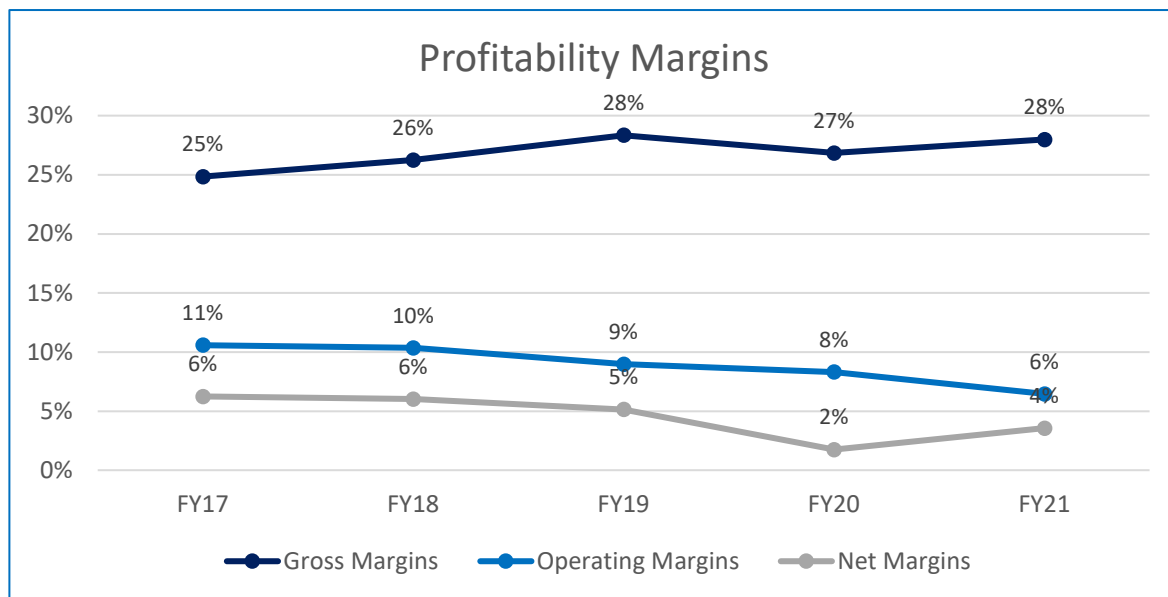
Export

- Amongst the exports, leather garments makeup ~34% of the total, followed by gloves (~31%), leather tanned (~19%), and leather footwear (~13%). The industry is expected to continue to be one of five key export-oriented sectors (alongside textiles, sports goods, surgical goods and carpets) due to the fact that several of Pakistan’s leather products enjoy duty free access to the European Union (which is the largest consumer of leather goods globally) under the EU’s Generalized Scheme of Preferences (GSP+).
- Germany, USA, UK, Spain, Netherlands, and France are the most common export destination for leather and leather products from Pakistan.

Exports (~PKR mln)			Top Exporters - FY21 (PKR mln)							
			Garments		Leather Gloves		Leather Tanned		Leather Footwear	
	FY20	FY21								
Leather Garments	39,450	45,888	Germany	12,766	USA	10,274	Italy	4,250	Germany	5,394
Leather Gloves	33,512	41,630	USA	6,062	Canada	5,495	Vietnam	3,301	Italy	2,789
Leather Tanned	29,001	25,790	Spain	3,520	Germany	4,138	China	3,097	USA	2,047
Leather Footwear	16,885	17,389	Netherlands	3,345	Poland	2,198	Hongkong	2,210	Netherlands	1,515
Other	1,618	2,650	UK	3,244	Sweden	2,098	Bangladesh	1,810	UK	1,115
Total	120,466	133,347	France	3,006	UK	1,582	Korea	1,202	Spain	736
			Belgium	1,615	Italy	1,365	Spain	1,075	France	621
			Russia	1,335	Spain	1,245	Indonesia	965	Belgium	367
			Italy	1,239	UAE	1,166	Germany	805	Yemen	256
			Poland	1,198	France	1,128	South Africa	696	Afghanistan	226
			Others	8,558	Others	10,940	Others	6,378	Others	2,325
			Total	45,888	Total	41,630	Total	25,790	Total	17,389

Business Risk: Margins & Cost Structure

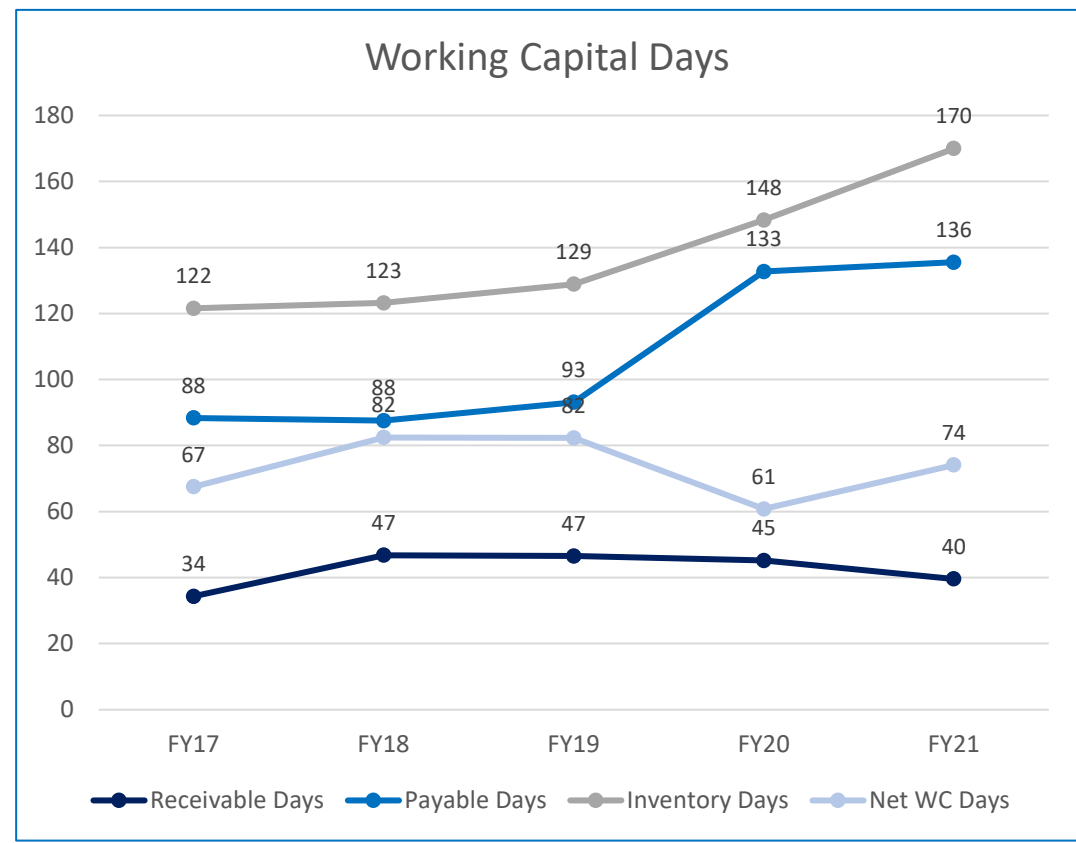
- Gross margins of leather sector have remained largely stable in the recent years, hovering within the range of ~25%-28%. The gross margins dipped slightly to ~27% (~28% in FY19) and net margins declined to ~8% in FY20 (9% in FY19) due to the low business activity in Europe caused by the COVID-related recession grips, and shift of exports revenue from India.
- With the resumption in economic activities, gross margins restored to ~28% in FY21. However, operating margins failed to recover and instead declined further to ~6% in FY21 majorly because both air and sea freight charges increased significantly due to COVID.
- Net margins improved to ~4% in FY21 (~2% in FY20) owing to historically low interest rates.
- Raw and packing material constitute ~67% of the total COGS, followed by salaries and wages (~10%) and fuel costs (~5%).



Note: Calculations are based on financials of 2 listed and 1 PACRA-rated client.

Financial Risk

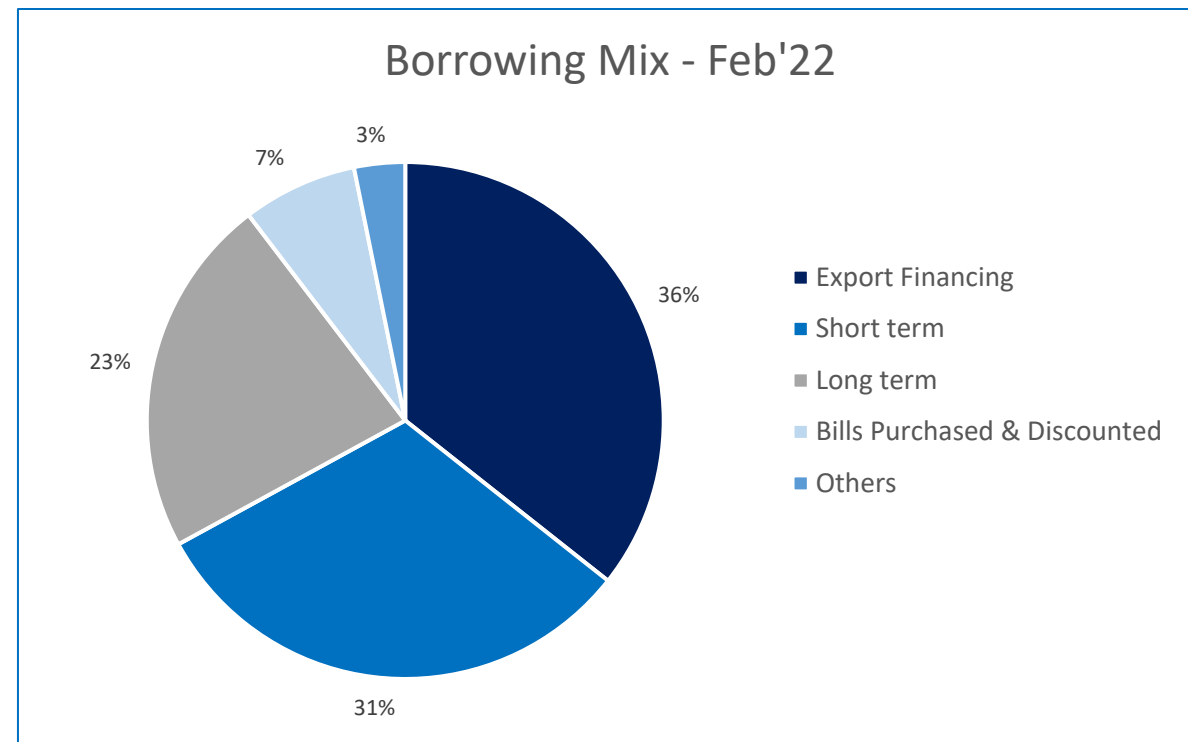
- Net working capital days of the sector were recorded at 74 days up ~21% YOY (FY20: 61 days).
- Net working capital days of the sector increased due to increase in inventory days. The suppliers had to maintain higher inventory levels in order to meet demand as the declining share of exports from India due to lockdown in FY21 shifted to Pakistan.
- Receivable days of the sector were recorded at 40 days during FY21 (FY20: 45 days). Companies usually sell their products at a credit of more than one month.
- The disruptions in supply chain caused delays in payments to suppliers, resulting in an increase in trade payable days of the sector during FY20 (~133 days) and FY21 (~136 days), up from ~93 days in FY19.



Note: Calculations are based on financials of 2 listed and 1 PACRA-rated client.

Financial Risk

- According to SBP numbers, total outstanding debt of the sector was recorded around PKR~41,831mln at end-Feb'22, as compared to PKR~35,699 at end-Jun'21, depicting a growth of ~17%.
- Export financing constitute major portion (~36%) of the total debt as the sector is export oriented. This is followed by short term and long term borrowing that makeup ~31% and ~23% of the total respectively.
- The sector is moderately leveraged. Gearing ratio of the sector was recorded at ~40% during FY21 (FY20: ~39%).



Note: Calculations are based on financials of 2 listed and 1 PACRA-rated client.

Tax and Regulatory Structure

PCT Code	Description	Custom Duty		Additional Custom Duty		Regulatory Duty		Total	
		FY21	FY22	FY21	FY22	FY21	FY22	FY21	FY22
	Articles of apparel and clothing accessories, 42.03 of leather or of composition leather.	20%	20%	7%	7%	0%	0%	27%	27%
	Footwear with outer soles of rubber, plastics, leather or composition leather and uppers of 64.03 leather.	20%	20%	7%	7%	0%	0%	27%	27%
4202.112	Suit-cases, of leather or composition leather	20%	20%	7%	7%	0%	0%	27%	27%
4202.21	Handbags, whether or not with shoulder strap, including those without handle: With outer surface of leather or of composition leather	20%	20%	7%	7%	0%	0%	27%	27%
4202.31	Articles of a kind normally carried in the pocket or in the handbag: With outer surface of leather or of composition leather	20%	20%	7%	7%	0%	0%	27%	27%



SWOT Analysis

- Ample availability of raw material (hides and skins of animals) locally
- Export friendly government policies

Strengths

Weaknesses

- Insufficient degree of advanced technology, resulting in higher cost of production as compared to international competitors
- Lack of skilled labor force in the country
- Lack of strong presence in the global fashion market

- The introduction of low-priced alternatives, such as synthetic leather
- High concentration in the European market

Threats

Opportunities

- Increasing fashion consciousness, resulting in a new market for leather garments and footwear
- High untapped potential for exports in USA and China
- Depreciating PKR, resulting in increased revenue

Outlook: Stable

- Both Global and Pakistan's economy are on the path of recovery after the decline witnessed due to the COVID-19 pandemic, which caused suspension in international travel and trade, leading to restricted demand for leather products. Now, with significant relaxations in lockdowns in various countries and the government's prudent policies, the leather industry of Pakistan is witnessing steady recovery.
- The growing population, in confluence with increasing fashion consciousness and demand for comfortable fashion products are escalating the demand for leather products globally. Moreover, the growing interest in travelling is boosting the demand for leather products, especially travel and luggage bags. The inflating income levels of individuals, particularly after the COVID, is also expected to increase the demand for luxury and high-quality leather products.
- The fact that leather is one of the five export-oriented sector, and 80% of the sector comprises of SMEs, has made it a priority for government policies. In Sep 2021, government allowed the SME exporters to get financing from banks without any collateral security. The sector enjoys refund on sales tax as well. Moreover, the depreciating exchange rate has resulted in lower cost of Pakistani products in the international market.
- The hike in policy rate during FY22 by 250bps has increased the finance costs for the industry. The inflation level in the country is also consistently rising. The inflation rate accelerated to ~13% in Jan'22 as compared to ~5% in same period last year (Jan'21), and the growth is expected to remain in double digits in the near future, negatively impacting the disposable incomes, and hence the demand for high-quality and high-cost leather products.
- Going forward, the sector is expected to face challenges from regional competitors, particularly India, and increasing inflation and finance costs. However, depreciating exchange rate, support from government, and changing fashion trends are expected to keep the demand intact.

- Pakistan Bureau of Statistics (PBS)
- Pakistan Stock Exchange (PSX)
- State Bank of Pakistan (PBS)
- PACRA Database
- PR Newswire
- SOMO
- UN Comtrade
- PR Newswire
- Trade Map

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